Petition and Transcript of Record

Supreme Court of the United States

OCTOBER TERM, 1931

No. 560

CONTINENTAL TIRE AND LUMBER COMPANY, PETITIONER,

vs.

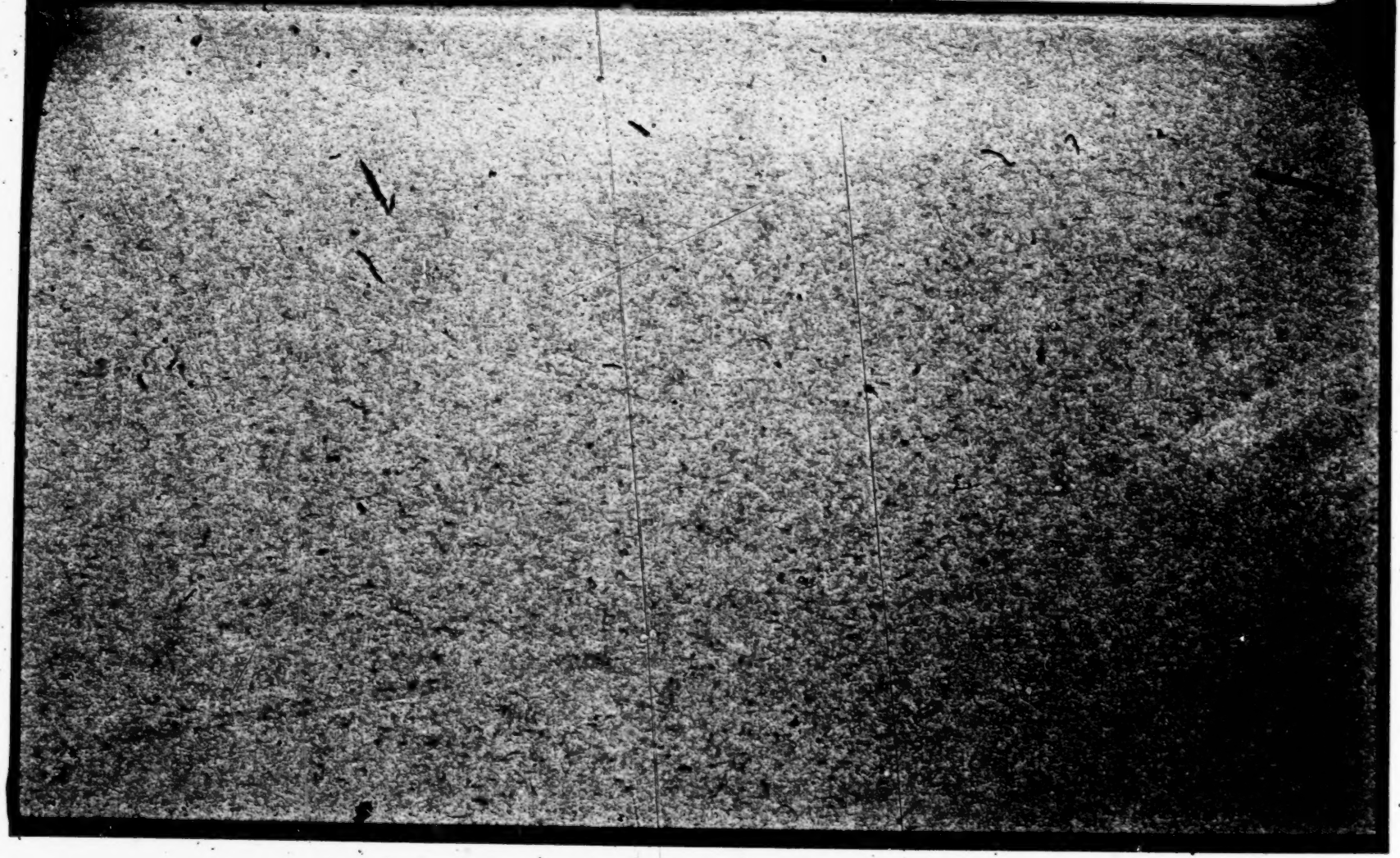
THE UNITED STATES

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

PETITION FOR CERTIORARI FILED DECEMBER 8, 1931

CERTIORARI GRANTED FEBRUARY 15, 1932

(36,374)



(36,374)

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[fol. 1]

IN SUPREME COURT OF THE UNITED STATES

No. 560

CONTINENTAL TIE & LUMBER COMPANY, Petitioner,

v.

THE UNITED STATES OF AMERICA, Respondent

PETITION FOR WRIT OF CERTIORARI TO THE COURT OF CLAIMS OF THE UNITED STATES

Petitioner respectfully shows the Court:

A

Summary Statement of the Matter Involved

This is a petition for a Writ of Certiorari to the Court of Claims involving a decision by that Court rendered October 20th, 1931.

Petitioner is a corporation engaged in the lumber manufacturing business and with principal office at Denver, Colorado. In 1907 petitioner incorporated a logging railroad known as "The Cimarron and Northwestern Railway Company" and ever since that time has owned the entire capital stock of said railroad company.

Throughout the period December 28, 1917, to June 3rd, 1918, inclusive, the Cimarron and Northwestern Railway Company was in possession and control of and operated by the President of the United States, through the Director-General of Railroads. On the latter date the road was relinquished from Federal control by the Director-General.

On October 19th, 1923, the Cimarron and Northwestern [fol. 2] Railway Company received from the Treasurer of the United States the sum of $25,228.35 which was paid to it pursuant to the provisions of Section 204 of the Transportation Act of 1920.

Petitioner rendered a consolidated income tax return for itself and its subsidiary, the Cimarron and Northwestern Railway Company, for the year 1920. In auditing said

return the Commissioner of Internal Revenue included therein as income the aforesaid payment of $25,228.35.

In due time petitioner filed a claim for refund with the Commissioner of Internal Revenue wherein it was contended that said payment under Section 204 of the Transportation Act of 1920 did not constitute taxable income to the Cimarron and Northwestern Railway Company and should not be included in the consolidated net income. The Commissioner of Internal Revenue denied the claim and suit was instituted in the Court of Claims thereon. The Court of Claims agreed with the Commissioner of Internal Revenue and in decision entered October 20th, 1931, held that said amount constituted taxable net income to the Cimarron and Northwestern Railway Company in the year 1920 and should be included in the consolidated net income for said year.

B

Reasons Relied Upon for the Allowance of this Writ

1. Payments to carriers under the provisions of Section 204 of the Transportation Act of 1920 do not constitute taxable income as defined by this Court.

[fol. 3] This Court has held that income is the "gain derived from capital, from labor, or from both combined," including the "profit gained through a sale or conversion of capital assets." Eisner v. Macomber, 40 S. Ct. 189, 252 U. S. 189.

The payment under Section 204 was a gratuity and did not represent gains or profits to petitioner from capital or labor or from the sale of its capital assets.

2. Payments Under Section 204 of the Transportation Act of 1920 do not Constitute Taxable Income because They were not paid Pursuant to any Existing Contract.

The fundamental test of income taxation is that income can arise only through contract, although not all contracts give rise to income.

3. The decision of the Court of Claims is Directly in Conflict with the Decisions of this Honorable Court.

In Edwards v. Cuba Railroad Company, 268 U. S. 628, it was held that money subsidies and property paid to the railroad by the Republic of Cuba were not taxable income

even though they were made upon the express stipulation and understanding that the railroad must extend its lines into new territory. In the instant case the railroad or carrier was not obligated to do anything as a condition to receiving said payment.

4. The Decision of the Court of Claims is in direct conflict with the holdings of the Interstate Commerce Commission upon the Question Involved.

In Finance Docket No. 1176, the Interstate Commerce Commission held that payments to railroads under Section [fol. 4] 209 of the Transportation Act were gratuities (even though the railroads were required to enter into an agreement with the Government to pay over to the Government a certain amount in excess of a stipulated earning). If payments under Section 209 were gratuities, how much more would this be true of payments under Section 204 where no agreements at all were required from the carrier and where it was required to pay nothing over to the Government.

5. This petition for Certiorari should be Granted Because there are Numerous Other Claims Pending before the Internal Revenue Bureau, the Board of Tax Appeals, and the Courts involving the same issue, which will be controlled by the decision herein.

This question must ultimately be decided by this Honorable Court and it would seem unfair to defer such action thus depriving this petitioner of the benefit of this Court's decision.

Wherefore your petitioner prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the United States Court of Claims commanding that Court to certify and transmit to this Court for review and determination, on a day certain to be therein named, a full and complete transcript of the record and of the proceedings in the case numbered and entitled on its docket as No. J-597, Continental Tie and Lumber Company, Plaintiff, v. The United States, Defendant; and that said judgment as to the item of $25,228.35 here in controversy be reversed by this Honorable Court and that your petitioner may have such other and further relief in the

[fols. 5 & 6] premises as to this Honorable Court may seem meet and just; and your petitioner will ever pray.

Continental Tie & Lumber Company, Petitioner, by Geo. E. H. Goodner, Counsel for Petitioner.

[fol. 1] IN THE COURT OF CLAIMS

No. J-597

CONTINENTAL TIE AND LUMBER COMPANY, Plaintiff,

v.

UNITED STATES OF AMERICA, Defendant

I. PETITION—Filed August 29, 1928

To the Honorable the Chief Justice and the Judges of the Court of Claims:

Plaintiff respectfully represents to the Court:

1. That this action is brought in this Court under authority of Section 145 of the Judicial Code.

2. That plaintiff is a corporation organized in 1905 and existing under the laws of the State of Colorado with principal office at Denver, Colorado; that ever since organization it has been engaged in the lumber manufacturing business.

3. That it incorporated its logging railroad in 1907 as the Cimarron and Northwestern Railway Company and ever since that time it has owned and controlled all of the capital stock of said Company.

4. That pursuant to the provisions of Section 240 of the Revenue Act of 1918, and the regulations promulgated thereunder by the Treasury Department, plaintiff and the said Cimarron and Northwestern Railway Company filed with the Collector at Denver, Colorado, a consolidated in-[fol. 2] come tax return for 1920 and plaintiff, as the parent or principal company, paid the tax assessed thereon of $3,207.06; that on February 23, 1926, plaintiff filed with said Collector a refund claim, prepared on Treasury Department Form 843, demanding refund of $2,995.49 of the

tax paid by it for 1920; that upon consideration of said claim the Commissioner of Internal Revenue agreed to and allowed all of the contentions made in said claim, except for one small item of $100.00 in deductions, which action would have resulted in the allowance of all the refund claimed, except $10.00, but for the fact that the said Commissioner then for the first time included in income for said year the sum of $27,228.35, which reduced the refund to $262.65; that the said Commissioner notified plaintiff of such action by letter dated September 20, 1926, and thereafter refunded the $262.65.

5. That said sum of $27,228.35 represented money paid to the Cimarron and Northwestern Railway Company in 1923 by the Railroad Administration under the provisions of Section 204 of the Transportation Act of 1920; that no part of said sum was received by said Company in 1920 or accrued on its books during that year; that no part of it was taxable income either to said Railroad Company or to plaintiff; and that all of said payment was an outright gift or donation to said Company.

6. That on March 15, 1927, plaintiff filed with the Collector at Denver, Colorado, a refund claim prepared on Treasury Department Form 843, demanding refund of $2,722.84 of the tax paid for 1920, a copy of which claim is attached hereto, made a part hereof, and marked "Exhibit A"; that said Commissioner rejected said claim in [fol. 3] full and notified plaintiff of such by letter dated May 28, 1927.

7. That, due to the erroneous inclusion in income by the Commissioner of Internal Revenue of the $27,228.35 as herein stated, plaintiff has overpaid its tax by the sum of $2,722.84, no part of which has been refunded and all of which is still retained by the United States.

8. That plaintiff is the sole owner of said claim; that no action other than as aforesaid has been had on this claim in Congress, in the Courts, or in any of the Executive Departments of the Government; that no transfer or assignment of said claim or any interest therein has been made; and that plaintiff is justly entitled to the refund now sought after allowing all just credits and set-offs.

9. That plaintiff has at all times borne true allegiance to the Government of the United States, and that it has not

in any way aided, abetted, or given encouragement to rebellion against said Government.

10. That plaintiff believes the facts stated herein are true.

Wherefore, plaintiff prays judgment against the United States for the sum of $2,722.84, together with interest thereon at 6% per annum from date of payment as provided by law.

Continental Tie and Lumber Company, Plaintiff, by Geo. E. H. Goodner, Attorney.

Address: Munsey Building, Washington, D. C.

[fol. 4] *Duly sworn to by Geo. E. H. Goodner. Jurat omitted in printing.*

[fol. 5] EXHIBIT "A" TO PETITION

(Execute Separate Form for Each Tax Period)

Claim for

Abatement of Tax Assessed
Credit Against Outstanding Assessments
XXX Refund of Taxes Illegally Collected
Refund of Amounts Paid for Stamps
Used in Error or Excess

STATE OF COLORADO,
County and City of Denver, ss:

Continental Tie & Lumber Company, Chamber of Commerce Building, Denver, Colorado.

This deponent, being duly sworn according to law deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below with reference to said statement are true and complete:

Period	Year
From	Jan. 1, 1920
To	Dec. 31, 1920

1. Business in which engaged: Timber and manufacturing lumber.
2. Character of assessment or tax: Income and profits.
3. Amount of assessment or stamps purchased: $2,944.41.
4. Reduction of Tax Liability requested (Income and Profits Tax): $2,722.84.
5. Amount to be abated: $——.
6. Amount to be refunded (or such greater amount as is legally refundable): $2,722.84.
7. Dates of payment (See Collector's receipts or indorsements of canceled checks) 1921.

(If statement covers income tax liability, items 8-11, inclusive, must be answered.)

8. District in which return (if any) was filed: Colorado.
9. District in which unpaid assessment appears: ——

[fol. 6] 10. Amount of overpayment claimed as credit: $——.

11. Unpaid assessment against which credit is asked; period from —— to ——, $——.

Deponent verily believes that this application should be allowed for the following reasons:

See attached sheets 1 to 4 made a part hereof.

(Sgd.) T. A. Schomburg, President.

Rec'd original hereof 3-15-27. By (Sgd.) George T. Evans, Collector of Int. Rev.

Sworn to and subscribed before me this 15th day of March, 1927. My commission expires Dec. 15, 1927. (Sgd.) Anna E. Allen, Notary Public.

On February 23, 1926, taxpayer filed with the Collector at Denver, Colorado, a refund claim demanding refund of $2,995.49 for the year 1920. Upon examination of said claim the Commissioner agreed to all the adjustments claimed and set forth therein except as to a difference of $100.00 in depreciation not now in dispute. But the Commissioner added to income an item not theretofore included in income and therefore not mentioned in said claim. This item is $27,228.35, the amount received by the Cimarron & Northwestern Railway Company, a subsidiary of taxpayer, in 1923, under Section 204 of the Transportation

Act of 1920. The Commissioner holds that this amount was taxable income in 1920. His determination of income and tax liability and action on said claim is set forth in Bureau letter dated September 20, 1926, Symbols IT:CR:G-5-SMC, resulting in an overassessment for 1920 of $262.65. [fol. 7] But for said addition to income, the overassessment would have been $2,985.49, which in effect is the payment of an additional tax by taxpayer because of this new item not before put at issue. In other words, the Commissioner allowed taxpayer's claim as filed (except for the $100.00 difference in income), but proceeded to offset $2,722.84 of the refund by additional tax from an entirely new source and on an entirely new basis, upon which taxpayer has never been heard.

On the basis of the foregoing facts, taxpayer claims the right to file this refund claim under the provisions of Section 284(a) and (b) of the Revenue Act of 1926 (being within four years from said constructive payment of additional tax), and also under the provisions of Section 284(g) of the Revenue Act of 1926, in that a waiver for 1920 was filed with the Commissioner on September 15, 1925, a copy of which waiver is attached hereto and made a part hereof. Furthermore, taxpayer offers this claim as supplemental to and amendatory of said claim filed on February 23, 1926, which said claim is by reference made a part hereof, for the reason that in considering said claim, the Commissioner raised a new issue for the first time which he made the basis of additional tax, and to deny taxpayer the right to file this claim and have it considered would be depriving it of the right to be heard and depriving it of property without due process of law.

Taxpayer denies that the $27,228.35, or any part of it, was taxable income in 1920 for the reason, first, that said payment did not constitute taxable income under the Revenue Act of 1918, and, second, that no part of said payment was received by taxpayer in 1920 and could not have been accrued in that year. Therefore taxpayer demands refund of $2,722.84, the amount of tax which the Commissioner is withholding from taxpayer on this issue, after allowing taxpayer's former claim of February 23, 1926, in full (except for the $100.00 difference in income), together with interest thereon as provided by law. The attached state-

ment shows the method of computing the tax liability and refund as claimed by taxpayer.

[fol. 8] An oral hearing is desired on this claim when it is reached for consideration in Washington, D. C., of which taxpayer's Attorney, Mr. Geo. E. H. Goodner, Munsey Building, Washington, D. C., should be notified.

STATEMENT

Continental Tie & Lumber Company, Cimarron & North-Western Railway Company

Consolidated Income and Tax Liability, 1920

Consolidated Net income stated in Revenue Agent's Report dated April 17, 1926, and Bureau Letter dated September 20, 1926		$31,444.05
Deduct amount received by Cimarron & Northwestern Railway Company under Section 204 of Transportation Act of 1920		27,228.35
Correct net income		$4,215.70

Tax

Net income as above	$4,215.70	
Exemption	2,000.00	
Balance taxable at 10%	$2,215.70	
Tax at 10%		$221.57
Tax assessed March, 1921 (#403310)	$3,207.06	
Overassessment allowed Bur. Letter 6/20/26	262.65	
		2,944.41
Overassessment now claimed as refund		$2,722.84

[fol. 9] (Copy)

(Form 872. 20

Treasury Department, Internal Revenue Service

89 Cole 1120, July 22, 1925.
Distribution Center, Sept. 15, 1925, Con. Ret. Division.

Income and Profits Tax Waiver for Taxable Years Ended Prior to January 1, 1922

Sept. 11, 1925.

In pursuance of the provisions of existing Internal Revenue Laws The Continental Tie and Lbr. Co., a taxpayer of ——, and the Commissioner of Internal Revenue hereby waive the time prescribed by law for making any assessment of the amount of income, excess-profits, or war-profits taxes due under any return made by or on behalf of said taxpayer for the year 1920 and 1921 under existing revenue acts, or under prior revenue acts.

This waiver of the time for making any assessment as aforesaid shall remain in effect until December 31, 1926, and shall then expire except that if a notice of a deficiency in tax is sent to said taxpayer by registered mail before said date and (1) no appeal is filed therefrom with the United States Board of Tax Appeals then said date shall be extended sixty days, or (2) if an appeal is filed with said Board then said date shall be extended by the number of days between the date of mailing of said notice of deficiency and the date of final decision by said Board.

The Continental Tie & Lumber Company, by (Signed) Fred F. Dehn, Assistant Secretary, Taxpayer. By (Signed) S. H. Blair, Commissioner.

OK. HBR.

[fol. 10] If this waiver is executed on behalf of a corporation, it must be signed by such officer or officers of the corporation as are empowered under the laws of the State in which the corporation is located to sign for the corporation, in addition to which, the seal, if any, of the corporation must be affixed.

[fol. 11] II. General Traverse—Filed Oct. 8, 1928

And now comes the Attorney General, on behalf of the United States, and answering the petition of the plaintiff herein, denies each and every allegation therein contained; and asks judgment that the petition be dismissed.

Herman J. Galloway, Assistant Attorney General.

III. Argument and Submission of Case

On February 11, 1931, this case was argued and submitted on merits by Mr. George E. H. Goodner, for the plaintiff, and by Mr. Assistant Attorney General Charles B. Rugg, for the defendant.

[fol. 12] **IV. Special Findings of Fact, Conclusion of Law, and Opinion of the Court by Littleton, J.** —Filed October 20, 1931.

Mr. George E. H. Goodner for the plaintiff.

Mr. Assistant Attorney General Charles B. Rugg for the defendant.

Mr. Lisle A. Smith and Mr. George D. Brabson were on the brief.

This suit was brought to recover $2,722.84, income tax alleged to have been erroneously and illegally collected for 1920, with interest.

The questions are whether in computing taxable income for 1920 on the accrual basis there should be included herein (1) $2,000 paid June 28, 1923, by the Director General of Railroads in settlement of claims arising through Federal control during the period December 28, 1917, to June 3, 1918, inclusive, and (2) $25,228.35 paid by the United States October 19, 1923, pursuant to section 204 of the transportation act of 1920 for reimbursement of deficits during Federal control.

Plaintiff contends that the first item was not income in 1920 and that the second item was not income at all since it was compensation to the carrier arising out of Federal

control which was a gratuity or bounty which was not taxable under the act of 1918.

Special Findings of Fact

1. Plaintiff, a Colorado corporation organized in 1905 with principal office at Denver, was during the taxable year, and had been since its organization, engaged in the lumber-manufacturing business. In 1907 it incorporated a railroad known as the Cimarron and Northwestern Railway Company, and since that year it has continuously owned the entire capital stock of said railroad. For 1920 it filed a consolidated tax return for itself and its subsidiary and paid the tax of $3,207.06 shown thereon in four installments of $800.76 each on March 16 and September 12, 1921, and $801.77 each on June 13 and December 13, 1921.

2. February 23, 1926, plaintiff filed a claim for refund for 1920 of $2,995.49. This claim was duly considered by the commissioner and he agreed and allowed all adjustments claimed and set forth therein except an item of $100 for depreciation which is not now in dispute.

[fol. 13] 3. In the final audit of the return for 1920 the commissioner determined a total consolidated net income of $31,444.05 and a total tax liability of $2,944.41, but included for the first time in plaintiff's income for 1920 the sum of $27,228.35, which inclusion increased plaintiff's income tax for 1920 and reduced the amount of the refund under the claim to $262.65. By letter of September 20, 1926, the commissioner notified the plaintiff of his action and subsequently plaintiff received and accepted a refund of $262.65.

4. The Cimarron & Northwestern Railway Company was in possession and control of and operated by the President of the United States through the Director General of Railroads from December 28, 1917, to June 3, 1918, inclusive, and was relinquished from Federal control by the Director General by his order to the carrier dated June 3, 1918. In arriving at the total net income of $31,444.05, the Commissioner of Internal Revenue included therein $2,000 which was paid to the railway company by the Director General of Railroads on June 28, 1923, pursuant to the final settlement agreement between the Director General and the rail-

way company. A copy of this agreement is in evidence as Exhibit 1 and is made a part hereof by reference.

In arriving at the total consolidated net income aforesaid, the Commissioner of Internal Revenue also included therein $25,228.35, which was the amount paid to the railway company by the Treasurer of the United States on October 19, 1923, under the following circumstances: (a) March 4, 1920, the Interstate Commerce Commission issued an order pursuant to the provisions of section 204 of the transportation act of 1920 and soon thereafter forwarded to the Cimarron & Northwestern Railway Company a form entitled "Report of Deficit Roads under Section 204 of the Transportation Act, 1920," containing appropriate instructions for furnishing the information called for; (b) November 3, 1922, the carrier filed with the Interstate Commerce Commission the information and data requested in said form, giving a summary by months of the carrier's operating income or deficit for the test period of three years from July 1, 1914, to July 1, 1917, and also the operating deficit for the period from January 1, 1918, to February 29, 1920. An accountant for the Interstate Commerce Commission made an inspection of the carrier's accounts and determined that the net credit in carrier's favor for the period June 4, 1918, to February 29, 1920, was $42,594.76; (c) the Bureau of Finance of the Interstate Commerce Commission then considered the carrier's claim, and notified carrier by letter dated April 12, 1923, that no amount remained to be certified to its credit under said act on the information before the bureau, but allowed the carrier to submit additional data as to relative costs between the test period and the period of Federal control during which it operated its own road, this evidence to be considered in deriving a factor which might be applied to the carrier's claim and furnish a basis for its allowance; (d) said additional information was furnished by the carrier, and on October 13, 1923, the Interstate Commerce Commission certified to the Secretary of the Treasury that the carrier, The Cimarron & Northwestern Railway Company, was entitled to the sum of $25,228.35, under section 204 of the transportation act [fol. 14] of 1920, said certificate being based on the report and decision of the commission dated October 13, 1923.

The commission in its decision of October 13, 1923, find-

ing the aforementioned amount of $25,228.35 due the subsidiary of plaintiff, stated:

The Cimarron & Northwestern Railway Company, a corporation of the State of New Mexico, hereinafter termed the carrier, is a steam railroad company which, during the Federal control period, engaged as a common carrier in general transportation, operating a line of railroad between Cimarron and Ponil Park, N. Mex., approximately 27 miles, which connected with the Atchison, Topeka & Santa Fe Railway, a railroad under Federal control. It sustained a deficit in its railway-operating income while under private operation in the Federal control period. It is, therefore, a carrier within the meaning of paragraph (a) of section 204 of the transportation act, 1920.

The carrier was under Federal control from January 1, 1918, to June 3, 1918, inclusive, and is entitled to the benefits of section 204 for the period from June 4, 1918, to February 29, 1920, inclusive. Its return under our circular of March 4, 1920, indicated a net credit of $45,090.57 in its favor for the period from January 1, 1918, to February 29, 1920, inclusive. Our examination of its accounts for the period from June 4, 1918, to February 29, 1920, inclusive, shows the net credit to the carrier for that period to be $42,594.76 before making the adjustments under the provisions of paragraph (f) of section 209, required by paragraph (b) of section 204.

Consideration has been given by us to the adjustment of maintenance charges and applying, so far as practicable, the rule set forth in the proviso of paragraph (a) of section 5 of the standard contract between the director general and carriers under Federal control, we have disallowed $17,366.41 of the maintenance expenditures for the period in question.

We find that there is payable to the carrier under paragraphs (f) and (g) of section 204 of the transportation act, 1920, the sum of $25,288.35 from which no amount is deductible as due to the President, as operator of transportation systems under Federal control, on account of traffic balances or other indebtedness. The carrier has expressed its willingness to accept this amount in final settlement of all its claims against the United States under that section.

An appropriate certificate will be issued.

A copy of this certificate is in evidence as Exhibit 2 and is made a part hereof by reference.

5. The plaintiff and its subsidiary, the Cimarron & Northwestern Railway Company, kept their books and rendered their tax returns on the accrual basis, but did not include the amount of $25,228.35 in the return for 1920 or any subsequent year.

September 15, 1925, plaintiff filed with the commissioner an income and profits tax waiver extending the time for making assessment of any additional tax for 1920 until December 31, 1926.

6. March 15, 1927, plaintiff filed a claim for refund for 1920 of $2,722.84. This claim is in evidence as Exhibit A and is made a part hereof by reference. The commissioner rejected this claim in full and notified the plaintiff of his action May 28, 1927.

7. Plaintiff is the sole owner of the claim here involved and no assignment thereof or any interest therein has been [fol. 15] made, and no action other than as aforesaid has been had in Congress, in the courts, or in any of the executive departments of the Government.

Conclusion of Law

Upon the foregoing special findings of fact, which are made a part of the judgment herein, the court decides, as a conclusion of law, that the plaintiff is entitled to recover $200, with interest.

It is therefore adjudged and ordered that the plaintiff recover of and from the United States the sum of two hundred dollars ($200), with interest at the rate of 6 per cent per annum from December 13, 1921, to such date as the Commissioner of Internal Revenue may determine in accordance with the provisions of section 177 (b) of the Judicial Code, as amended by section 615 of the revenue act of May 29, 1928.

Opinion

Littleton, Judge, delivered the opinion of the court:

The Federal control act provided for the taking over of railroads and the payment of just compensation for the use thereof. The Cimarron & Northwestern Railway Com-

pany was taken over December 28, 1917, and turned back June 3, 1918. The company was paid certain sums at various times but final settlement with the Director General of Railroads was not made until 1923. In that year the company agreed to accept and the Director General paid $2,000 as settlement in full of all claims of the company arising out of Federal control of said railway.

Plaintiff contends that on the accrual basis this amount was income for 1918 but that if it was not income for 1918 it was not income until 1923. Nothing took place in 1920 to fix the accrual in that year. The amount was neither earned, determined, agreed to, nor paid in that year. We are of opinion that this item was not income in 1920. Illinois Terminal Co., 5 B. T. A. 15. Cincinnati, Findlay & Fort Wayne Railway Co., 5 B. T. A. 108. Virginia Carolina Securities Corporation, 6 B. T. A. 84. New Orleans, Texas & Mexico Railway Co., 6 B. T. A. 436. Great Northern Railway Co., 8 B. T. A. 225. Chicago, Rock Island & Pacific Ry. Co., 13 B. T. A. 988. Old Dominion Steamship Co., 16 B. T. A. 264. Kansas City Southern Ry. Co., 16 B. T. A. 665.

With reference to the second item of $25,228.35 paid to the plaintiff by the United States under section 204 of the transportation act of 1920 to make good the deficit of the plaintiff in its operating income for the guaranty period, January 1, 1918, to February 29, 1920, plaintiff contends that this payment was not income within the meaning of the taxing act but was a gratuity or bounty; that it did not arise through any legal obligation of the Government to pay; that it did not arise through contract; and that it was not a gain derived from capital or labor and was not determined, fixed, or allowed until 1923.

Section 204 of the transportation act, approved February 28, 1920, 41 Stat. 456, 460, entitled "Reimbursement of Deficits During Federal Control" provided:

[fol. 16] "Sec. 204. (a) When used in this section—

"The term 'carrier' means a carrier by railroad which, during any part of the period of Federal control, engaged as a common carrier in general transportation, and completed for traffic, or connected, with a railroad under Federal control, and which sustained a deficit in its railway operating income for that portion (as a whole) of the period of Federal control during which it operated its own railroad or system of transportation; but does not include

any street or interurban electric railway which has as its principal source of operating revenue urban, suburban, or interurban passenger traffic or sale of power, heat, and light, or both; and

"The term 'test period' means the three years ending June 30, 1917.

"(b) For the purposes of this section—

"Railway operating income or any deficit therein for the period of Federal control shall be computed in a manner similar to that provided in section 209 with respect to such income or deficit for the guaranty period; and

"Railway operating income or any deficit therein for the test period shall be computed in the manner provided in section 1 of the Federal control act.

"(c) As soon as practicable after March 1, 1920, the commissions shall ascertain for every carrier, for every month of the period of Federal control during which its railroad or system of transportation was not under Federal operation, its deficit in railway operating income, if any, and its railway operating income, if any (hereinafter called 'Federal control return') and the average of its deficit in railway operating income, if any, and of its railway operating income, if any, for the three corresponding months of the test period taken together (hereinafter called 'test period return'): Provided, That 'test period return,' in the case of a carrier which operated its railroad or system of transportation for at least one year during, but not for the whole of, the test period, means its railway operating income, or the deficit therein, for the corresponding month during the test period, or the average thereof for the corresponding months during the test period taken together during which the carrier operated its railroad or system of transportation.

"(d) For every month of the period of Federal control during which the railroad or system of transportation of the carrier was not under Federal operation, the commission shall then ascertain (1) the difference between its Federal control return, if a deficit, and its test period return, if a smaller deficit, or (2) the difference between its test period return, if an income, and its Federal control return, if a smaller income, or (3) the sum of its Federal control return, if a deficit, plus its test period return, if an

income. The sum of such amounts shall be credited to the carrier.

"(e) For every such month the commission shall then ascertain (1) the difference between the carrier's Federal control return, if an income, and its test period return, if a smaller income, or (2) the difference between its test period return, if a deficit, and its Federal control return, if a smaller deficit, or (3) the sum of its Federal control return, if an income, plus its test period return, if a deficit: [fol. 17] The sum of such amounts shall be credited to the United States.

" (f) If the sum of the amounts so credited to the carrier under subdivision (d) exceeds the sum of the amounts so credited to the United States under subdivision (e), the difference shall be payable to the carrier. In the case of a carrier which operated its railroad or system of transportation for less than a year during, or for none of, the test period, the foregoing computations shall not be used, but there shall be payable to such carrier its deficit in railway operating income for that portion (as a whole) of the period of Federal control during which it operated its own railroad or system of transportation.

" (g) The commission shall promptly certify to the Secretary of the Treasury the several amounts payable to carriers under paragraph (f). The Secretary of the Treasury is hereby authorized and directed thereupon to draw warrants in favor of each such carrier upon the Treasury of the United States for the amount shown in such certificate as payable thereto. An amount sufficient to pay such warrants is hereby appropriated out of any money in the Treasury not otherwise appropriated."

The foregoing section was enacted for the benefit of only those railroads engaged as common carriers which had connection with and competed with railroads under Federal control. The benefits of the section were designed not for all such carriers but only those which suffered a genuine deficit in operating income by reason of traffic diversions and other practices of the Railroad Administration. The general intent of the section was to afford relief to carriers which through their service were entitled by the public interest to preservation as a part of the transportation sys-

tem of the country and the specific purpose of the section was to reimburse such railways on account of deficits in their net railway operating income. The legislative history shows that it was the intention of Congress to extend certain aid to railways not under Federal control consisting largely of so-called short lines, in recognition not only of their financial necessities but of injury to them through Federal control and operation of lines with which they connected or competed during the Federal control period.

To sustain a claim under this section a railroad must not only have engaged as a common carrier in general transportation but must have competed for traffic or connected with a railroad under Federal control.[1]

Section 204 differs from section 209 considered by the court in Texas & Pacific Railway Co. v. United States, K-148, decided this date, in that it relates to reimbursements of deficits of railroads, during any part of the period of Federal control, engaged as a common carrier in general transportation, and competed for traffic, or connected, with a railroad under Federal control, which sustained a deficit in its railway-operating income for that portion, as a whole, of the period of Federal control in which it operated its own railroad or system of transportation, but we think the [fol. 18] same reasons which lead to the conclusion that amounts received by railroads from the Government pursuant to section 209 of the transportation act are income subject to taxation under the revenue acts apply to amounts paid by the Government under section 204. We find no reason to assume that Congress intended section 209 as a compensation provision and section 204 as a gratuity or bounty provision. Although in section 204 there is absent the contractual relationship between the carrier and the Government found in section 209, this does not, in our opinion, warrant the conclusion that section 204 was designed to confer a gift or gratuity upon railroads since any

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[1] Little Cottonwood Company, 65 I. C. C. 189; Mercer Valley R. R. Co., 76 I. C. C. 55; United States and C. R. Co., 76 I. C. C. 455; Manitou & Pacific Railway Company, 94 I. C. C. 767; Bingham & G. Railway Co., 99 I. C. C. 724; Rural Valley Railroad Company, 131 I. C. C. 509; Glenfield & Western Railroad Company, 150 I. C. C. 39.

amount payable thereunder arose from the operation of the railroad by the carrier and the use of capital and labor. We think the receipt by the carrier of an amount sufficient to reimburse it for a deficit in railway-operating income computed in accordance with the provisions of section 204 of the transportation act falls within the definition of income under the sixteenth amendment and the revenue act of 1918 as defined by the Supreme Court. The entire phraseology of the transportation act is directed toward the idea of compensation and a consideration of its history and purpose shows that section 204 was designed to reimburse or compensate particular carriers which had suffiered by reason of the policies and practices of the Railroad Administration through traffic diversions and divisions.

We think there is no merit in the contention of the plaintiff that the amount of $25,228.35 paid to the Cimarron and Northwestern Railway Company by the United States should not be included in income until determined and paid in 1923. The amount represented a deficit in railway-operating income for that portion, as a whole, of the period of Federal control during which the Cimarron and Northwestern Railway Company operated its own rairoad or system of transportation. It kept its books on the accrual basis. Prior to the enactment of the transportation act on February 28, 1920, no right in the Cimarron and Northwestern Railway Company to the receipt of this amount existed. The right to receipt accrued upon the termination of Federal control on March 1, 1920. All that remained to be done was to compute the deficit in accordance with the provisions of the act. The accrual system of accounting, as it has always been applied, requires time for computation and adjustment. The plaintiff had previous knowledge and experience as to the test period whereby the railway-operating income and deficit were to be measured and the transportation act was enacted in ample time for the necessary computations to have been made or reasonably estimated for the purpose of accrual in 1920. No contention is made as to any question of dispute or difference between the parties which might have made an estimate or accrual of the claim of the Cimarron and Northwestern Railway Company impossible. There appears to have been no substantial dispute between the plaintiff and the Interstate Commerce Commission as to its claim. The

authority of the commission consisted in a review and audit of plaintiff's books for the purpose of determining its operating deficit as compared with similar accounts during the test period. It is true that there was considerable delay in the payment of plaintiff's claim but that was due to the failure of plaintiff to report or to submit a complete statement of facts and full information to the commission in response to the circular issued by it.

[fol. 19] Plaintiff relies upon Lucas v. American Code Co., 280 U. S. 445. This case held simply that a taxpayer may not set up a reserve to take care of its own breach of contract where it denies all liability therefor. There was no breach of contract here, no dispute of fact or of law between the plaintiff and the commission, or between the plaintiff and any branch of the Government. Furthermore, the plaintiff in American Code Company was not a common carrier subject to interstate commerce regulations which prescribe its method of accounting. In the American Code Company case, supra, the court stated "It may be assumed that, since the company kept its books on the accrual basis, the mere fact that the exact amount of the liability had not been definitely fixed in 1919 would not prevent the deduction, as a loss in that year, of the amount later paid. But here there are other obstacles. Obviously, the mere refusal to perform a contract does not justify the deduction, as a loss, of the anticipated damages. * * * And, when liability is contested, the institution of a suit does not, of itself, create certainty of loss." We, therefore, conclude that the plaintiff and its affiliated companies are not entitled to exclude from consolidated income for 1920 the amount of the operating deficit of the Cimarron and Northwestern Railway Company for which that company received reimbursement from the United States under section 204 of the Transportation Act of 1920.

Judgment will be entered in favor of plaintiff for $200 with interest, as provided by law. It is so ordered.

Whaley, Judge; Williams, Judge; Green, Judge; and Booth, Chief Justice, concur.

[fol. 20] JUDGMENT

At a Court of Claims held in the City of Washington on the 20th day of October, A. D., 1931, judgment was ordered to be entered as follows:

Upon the special findings of fact, which are made a part of the judgment herein, the court decides, as a conclusion of law, that the plaintiff is entitled to recover.

It is therefore adjudged and ordered that the plaintiff recover of and from the United States the sum of Two hundred dollars ($200), with interest at the rate of 6 per cent per annum from December 13, 1921, to such date as the Commissioner of Internal Revenue may determine in accordance with the provisions of section 177 (b) of the Judicial Code, as amended by section 615 of the revenue act of May 29, 1928.

[fol. 21] Clerk's certificate to foregoing transcript omitted in printing.

Endorsed on cover: File No. 36,374. Court of Claims. Term No. 560. Continental Tie and Lumber Company, petitioner, vs. The United States. Petition for a writ of certiorari and exhibit thereto. Filed December 8, 1931. File No. 36,374.

SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed February 15, 1932

The petition herein for a writ of certiorari to the Court of Claims is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

(1708)